

INTERNAL REVENUE SERVICE
Director, Exempt Organizations

DEPARTMENT OF THE TREASURY
Pacific Coast Area (TE/GE)

c/o McCaslin Industrial Park
2 Cupanial Circle
Monterey Park, CA 91755
[REDACTED]

Date: [REDACTED]

Employer Identification Number:
[REDACTED]

Contact Person:
[REDACTED]

Contact Telephone Number:
[REDACTED]
[REDACTED]

CERTIFIED MAIL

Dear Applicant:

We have considered your application for exemption from Federal income tax as an organization described in section 501(c)(4) of the Internal Revenue Code.

The information submitted indicates that you were incorporated as a nonprofit corporation on [REDACTED]

FACTS:

Your Articles of Incorporation state that your purpose, "consists on promoting to the public savings plan depending on the possibilities of each person, not exceeding a thirty years time period. The customers will be developing through a multilevel marketing. After a customer has acquire a savings plan, he will have the obligation of contracting order savings plan through their social circle, the purpose of this network will be for it to reach the seventh level." (sic)

You are proposing to sell "savings plans" to low-income individuals who desire to buy a home or refinance a current home. An individual who wishes to take part in your savings plan must sign a contract that requires that the individual make monthly payments to your organization as well as enlist three other individuals to sign up for the savings plan. The monthly payments are calculated by dividing the total amount an individual needs by [REDACTED] months. There is an additional [REDACTED] % administrative fee added to this amount. A member must then enlist three more individuals who in turn must enlist three more individuals and so on until a total of [REDACTED] people (referred to as the seventh level) have signed up for the savings program. You state in your application that once a member reaches this seventh level, you will provide, in cash, the total amount of a member's savings plan.

The member, in turn, is supposed to use the money to buy a house or pay off an existing mortgage. A member must pledge his house as collateral to ensure that he makes all the remaining payments in his plan, including the 1% administrative fee.

ISSUE:

Does the organization qualify for exemption from Federal income tax as an organization described in section 501(c)(4) of the Code?

LAW:

Section 501(c)(4) of the Code allows for the exemption from Federal income tax "Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes."

Income Tax Regulation Section 1.501(c)(4)-1(2)(i) states that "an organization is operated exclusively for the promotion of social welfare if the organization is primarily engaged in promoting the common good and general welfare of the people of the community."

In *Commissioner of Internal Revenue v. Lake Forest, Inc.* 305 F.2d 814 (1962) the court held that a non-profit corporation formed to acquire and operate low-income housing cooperative was not exempt as a civic league or social welfare organization because it did not offer a program or service to benefit the community-at-large. The Court held that the organization was a private cooperative undertaken for the benefit of its members, enabling them to save for a home, to satisfy their own material ambitions.

Revenue Ruling 75-199, 1975-1 C.B. 160, holds that an organization formed to provide sick benefits for its members and pay death benefits to the beneficiaries of members did not qualify for exemption under section 501(c)(4) of the Code. The organization's income was derived principally from member dues. The ruling states that a membership organization of this type is essentially a mutual, self-interest type of organization whose benefit to the larger community is minor and incidental.

Revenue Ruling 81-58, 1981-1 C.B. 331, holds that a nonprofit police officer association whose primary activity is providing lump-sum retirement payments to its members will not qualify as a social welfare organization described in section 501(c)(4) of Code. The ruling holds that the organization is essentially a mutual, self-interest type organization.

DISCUSSION AND ANALYSIS:

You are attempting to develop a multilevel marketing operation. A member is required to make monthly payments to your organization and enlist other individuals to also sign up for a monthly payment contract. These persons must also enlist another persons who in turn must enlist more persons and so on until there are a total of contracts signed. After a member reaches this seventh level, he is eligible to receive the full amount of the proceeds from his account in order to purchase a home. The time to reach the seventh level is only governed by the aggressiveness of the member in selling the savings program to others. During this time the member continues to make payments on his contract.

You state that you are helping low-income people who are unable to purchase a home through conventional means, buy or refinance a home. A member is expected to make monthly payments to your organization in addition to making their own monthly rent payment for the dwelling in which they currently reside. This appears to be a financial burden for a low-income individual as they are in reality making two house payments a month.

Your activities are similar to the activities of the organizations mentioned in the above revenue rulings and court case in that you are operating for the benefit of your members, and not the community-at-large. Also, it is highly doubtful that an individual can attain the "seventh level" and thus receive back all the monthly payments that have been paid to your organization.

CONCLUSION:


It is the position of the Internal Revenue Service, based on the information submitted, that you do not qualify for exemption under section 501(c)(4) of the Code inasmuch as you are not operated exclusively for the promotion of social welfare as defined in the Code and regulations for section 501(c)(4).

You are required to file federal income tax returns on Form 1120.

If you are not in agreement with this proposed determination, we recommend that you request a hearing with our office of Regional Director of Appeals. Your request for a hearing should include a written appeal giving the facts, law, and any other information to support your position as explained in the enclosed Publication 892. You will then be contacted to arrange for a hearing. The hearing may be held at the office of Regional Director of Appeals, or if you request, at a mutually convenient District office.

If we do not hear from you within 30 days from the date of this letter, and you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies and will then become our final determination.

Sincerely yours,

A handwritten signature in cursive script that reads "Steven T. Miller".

Steven T. Miller
Director, Exempt Organizations

Enclosures:
Publication 892
Notice 1214